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NABE Outlook

NABE Macroeconomic Forecast

February 1989

This report presents the consensus forecast results made by a select panel of 59 professional forecasters drawn from the membership of the National Association of Business Economists. Most of the forecasts were made in late January or early February, following the release of 4th quarter GNP data. This survey is one of three taken regularly by NABE; the other surveys are the **Industrial Outlook** *and the* **Economic Policy** *surveys.*

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Highlights from the February Survey

* The median forecast of NABE's economic outlook panel has been raised slightly--real GNP growth is now expected to be 2.7 percent on a year-over-year basis, up from the 2.5 percent forecast made last November. This growth rate is right in line with trend growth in both the labor force and manufacturing capacity, resulting in an economy in which both the unemployment and capacity utilization rates are expected to stabilize at or near current levels (5.4 percent unemployment and 85 percent utilization).

* Real economic growth in 1988 came in at 3.8 percent, again on a year-over-year basis, right in line with our panel's expectations as reflected in its last two forecasts. Thus, the expected growth in 1989 represents a noticeable slowdown in the current economic expansion.

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* But the panel has scaled back the risk of a possible 1989-90 economic downturn. A significant majority (75 percent) of panel members still expects a recession sometime during the next two years, down from 88 percent in November. Interestingly, the proportion expecting a 1989 decline has dropped from 40 percent to 19 percent. Many of the born-again optimists on 1989 have postponed their recession to 1990.

* Inflation is expected to accelerate in 1989. On the basis of 4th quarter-to-4th quarter changes in Consumer Prices, inflation in 1989 is expected to be 4.8 percent, up from 4.3 percent in 1988. On the GNP deflator, inflation is expected to run at a 4.5 percent rate during 1989, not significantly changed from our last forecast and a continuation of the rate experienced in the last half of 1988. *An important factor in the respondents' inflation forecasts was*--no major surprise--*their projections for real economic growth. In general, those respondents with higher growth rates also had higher inflation rates, which were probably driven by assumptions of tighter capacity use and more labor shortages.*

* The "twin deficits" should post modest improvements later in 1989. The median forecast for the merchandise trade deficit is $120 billion, moderately better than the actual $137 billion deficit in 1988. The median Federal budget deficit for the current 1989 fiscal year is $155 billion, unchanged from the actual deficit in fiscal 1988. For fiscal 1990, the panel expects only a slight improvement to $135 billion, well above the $100 billion Gramm-Rudman-Hollings requirement.

* Actual changes in market interest rates appear to be outstripping the panel's estimates. The panel thought interest rates would drift up to slightly higher peak levels by mid-1989 and then begin to move lower. Three-month Treasury bill yields were expected to move up .80 percentage points from the 4th quarter 1988 average to 8.5 percent during the 2nd quarter. *(This rise has already occurred.)* The panel then expected rates to decline to a 4th quarter 1989 average of 7.8 percent. *The estimates of the highest quartile are much closer to the actual pattern of interest rates in the opening two months of 1989. This group of interest-rate bears expect Treasury bill rates to rise by another 60 basis points and then hold at the 9.10 percent level during the 2nd half of 1989.*

* Long-term interest rates, as reflected in 30-year Treasury bond yields, should post similar, but smaller, movements. The panel expected a rise from 9.00 percent at the outset of 1989 to a 2nd quarter peak of 9.30 percent, with a return to the 9.00 level at the end of 1989. The bearish quartile calls for 10.00 percent bond yields by year-end 1990.

A Successful "Soft Landing?"

The panel's February forecasts continue to show improvement in the 1989 outlook. The median forecast now calls for growth of 2.7 percent, up from 2.5 percent last quarter and 2.3 percent in the August forecast. The primary reason for the better performance is a more ebullient consumer sector. Growth in this important sector is now expected to be 2.5 percent for 1989, up significantly from the 2.0 percent expected last November. This is a reflection of the current high level of consumer sentiment as well as a continuation of the strong retail sales encountered during the past Christmas season.

The 2.7 percent growth in real GNP is close to what many economists feel is the long-term trend growth of the U.S. economy. Growth above this rate for an extended period of time could result in an acceleration of inflation, due to tightness in labor markets and manufacturing capacity utilization. Thus, although lower than the 3.8 percent growth experienced last year, the current median forecast represents a more sustainable and comfortable rate of expansion.

Sector Outlook

The stronger economic growth being forecast by the majority of our respondents is primarily a function of a more ebullient consumer sector. However, the forecasts for other sectors have also improved, as follows:

* Industrial production is now expected to rise by 3.4 percent, as opposed to 3.0 percent in the November forecast.

* Housing starts are now expected to average 1.44 million units, up slightly from the 1.40 million in the last forecast, despite expectations of higher interest rates in the current forecast.

* Auto sales should total 10.2 million units in 1989, a slight increase from the November estimate of 10.0 million, although the figures would still be down from last year's 10.5 million result. In addition, van and truck sales are expected to be 5.1 million, very close to the 1988 levels.

Quarterly Interest Rate Forecasts

Our panel provide us with a quarterly path for both short and long-term interest rates. The quarterly medians, along with the average of the upper and lower 25 percent, are shown below:

Table 1

Quarterly Interest Rate Projections

			Estimates			
		88Q4A	89Q1F	89Q2F	89Q3F	89Q4F
91 Day T-Bills	- median	7.7%	8.3%	8.5%	8.0%	7.8%
	- upper 25%		8.5	8.9	9.1	9.1
	- lower 25%		8.0	7.8	7.4	6.9
30 Yr. T-Bonds	- median	9.0%	9.0	9.3	9.2	9.0
	- upper 25%		9.3	9.7	9.9	10.0
	- lower 25%		8.9	8.9	8.7	8.4

A = Actual; F = Forecast

The Next Recession Continues to be Postponed

The vast majority of our panel has again postponed the expected arrival of the next recession. Fewer than 20 percent of respondents felt that a downturn would commence in 1989, but a majority of participants now feels that 1990 is the most likely year. However, a significant 75 percent of the business economists in our panel still feel that a recession will arrive sometime before the end of next year.

Table 2

Recession Estimates

Next Recession Begins In:	Percent of Respondents in:			
	May 1988	Aug 1988	Nov 1988	Feb 1989
1989	57.4%	47.3%	40.0%	19.2%
1990	31.5	41.8	48.3	55.8
1991	1.9	9.1	8.3	17.3
1992 or later	3.8	1.8	3.3	7.7

Table 3

Summary of NABE Median Forecasts

	1988 Actual	May 88 Survey	1989 Forecasts: Aug 88 Survey	Nov 89 Survey	Feb 89 Survey
Fourth-Quarter to Fourth-Quarter					
Real GNP	2.7%	2.0%	2.0%	2.2%	2.5%
Consumer Price Index	4.3%	5.0%	5.1%	5.0%	4.8%
Annual Averages					
Real GNP	3.8%	2.2%	2.3%	2.5%	2.7%
Personal consumption expend.	2.8%	2.0%	2.0%	2.0%	2.5%
Nonresidential fixed invest.	9.5%	2.5%	3.7%	4.3%	4.0%
Net exports (billions)	-$99.1	-$93	-$67	-$76	-$85
Nominal Magnitudes:					
Merchandise trade balance	-$137.0	-$130	-$120	-$120	-$120
Federal budget deficit (FY)	-$154.9	-$151	-$150	-$150	-$155#
Corporate profits (after-tax)	12.6%	4.7%	5.0%	5.2%	6.3%
Real Magnitudes:					
Unemployment rate (civilian)	5.5%	5.9%	5.6%	5.6%	5.5%
Industrial production	5.7%	2.9%	2.9%	3.0%	3.4%
Housing starts (millions)	1.49	1.49	1.41	1.40	1.44
Auto sales (millions)	10.6	10.0	10.0	10.0	10.2
Inflation and Interest Rates:					
Consumer price index	4.1%	4.7%	5.0%	5.0%	4.7%
GNP deflator	3.4%	4.2%	4.4%	4.4%	4.5%
Treasury bills (91 days)	6.7%	6.8%	7.4%	7.5%	8.0%
Treasury bonds (30 years)	9.0%	9.5%	9.6%	9.5%	9.2%

\# The panel's estimated Federal budget deficit for fiscal 1990 is $135 billion.

The February 1989 column is based on 59 responses received.

When Will the Next Recession Start?